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C O N F I D E N T I A L SECTION 01 OF 02 SANTO DOMINGO 006118

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SUBJECT: IMF POLICY PAPER - DRAFT SUMMARY OF THE DOMINICAN
ENERGY SECTOR

REF: A. REF. A SANTO DOMINGO 01606

[1](#)B. REF B. SANTO DOMINGO 05740

Classified By: EcoPol Counselor MMEIGS. Reason: 1.4 (d).

(1.) (SBU) This message forwards a draft IMF summary of the plan of the Dominican government for dealing with energy difficulties. The Dominican Republic is currently suffering localized power outages of up to 12 hours a day due to poor government management of the sector, low collection rates by the distribution companies, the high cost of imported petroleum and the non-payment of government subsidies. The current accumulated sector deficit is USD 507 million and is expected to reach USD 650 million by the end of 2005. After the inauguration of President Fernandez on August 15, the government borrowed USD 65 million from local banks to cover the costs of producing 70 percent of the country's electricity production, to continue subsidizing bottled gas and to buy time to develop a long-term plan for the energy sector. In consultation with the World Bank, IDB and USAID, the administration developed a comprehensive plan to address the current energy crisis and delivered the plan to President Fernandez in October (REF. B).

(2.) (C) The GODR energy plan calls for short term action until December 2005. The plan includes a timetable for: (i) reducing losses and improving collection rates; (ii) better targeting of subsidies; (iii) improving the regulatory framework; (iv) reducing the cost of electricity generation; (v) roll over arrears with private electricity companies; and (vi) managing the power rationing. Here is a basic outline of the plan:

- Reducing losses and improving collection rates.
With the collaboration of the distribution companies, an aggressive loss reduction and collection increase plan will be gradually implemented, aimed at improving the overall cash recovery index of the distribution companies. The loss target (for December 2005 of Ede-Norte/Sur being 27 percent (down from 36 percent, mid-2004) and for Ede-Este 32 percent (down from 37 percent, mid-2004). The collection rate target (for December 2005) of Ede-Norte/Sur being 95 percent (up from 85 percent, mid-2004) and for Ede-Este 93 percent (up from 81.5 percent, mid-2004).

- Better targeting of subsidies.
Subsidies are to be focused on the small consumers, restructuring the tariff in three steps (November 2004), (December 2004) and (February 2005), overall resulting in an average tariff increase of about 30 percent. A new distribution model will be developed for the PRA (Program to Reduce Blackouts) areas in order to improve and reduce the targeting of this subsidy (paid with hydro, electricity) focused at small consumers whose consumption is not measured (third quarter 2005).

Improving the regulatory framework.
Uncontrollable costs (fuel prices, currency exchange rate and inflation) are to be passed through automatically to the final consumer tariffs, applying the appropriate indexation on a monthly basis, as opposed to the former quarterly basis (February 2005). Regulatory policies will be amended in order to facilitate expedite fraud detection and reduction efforts. (first quarter 2005)

Reducing the cost of electricity generation.
The plan includes an attempt at reducing the cost of electricity generation through the renegotiation of some power supply contracts. With a potential price reduction of about 1.0 US cents/KWh, the plan includes the renegotiation of the CESP (Cogentrics) power purchase agreement contract with CDE (second quarter 2005), the SECLP (Smith-Enron) contract (third quarter 2005). Finally, an attempt will be made at renegotiating the terms of the so-called Acuerdo de Madrid (reduction of contract rates by generators in return for a one-time payment) (latest, December 2005).

Roll over arrears with private electricity companies.
In the short term, the plan is to roll over arrears and pay only the interest that accumulates on the debt (up to

December 2005). Total interest payments during year 2005 are, estimated at US\$60 million

Managing the power rationing.

Rationing of power will take place according to the collections of the various circuits. The level of rationing will be linked to the overall results of the plan, the 70 percent supply restriction to be reduced only when disbursement of public funds to cover the current deficit gap is reduced to manageable figures (third quarter 2005). The need for public funds to close the current deficit gap of the electricity sector during year 2005, as a result of a successful implementation of this comprehensive plan, has been estimated at USD 219 million (assuming exchange rate of RD 40/USD and oil price of USD 50/barrel). The monthly requirements to be included in the national budget for year 2005 are;

Year 2005	million USD	
Jan /Feb /Mar	39 / 31 / 30	
Apr / May / Jun	30 / 23 / 20	
Jul / Aug- / Sep	13 / 14 / 12	
Oct / Nov / Dec	10 / 0 / -3	
Net Total		219

(3.) (C) In the medium and longer term, the plan includes actions for: (i) clearing arrears with private electricity companies; (ii) private sector participation in Ede-Norte/Sur distribution companies; and (iii) reforming the regulatory and legal framework of the sector. The details follow:

Clearing arrears with private electricity companies.
The external financing required will be procured (late 2005), so as to develop a plan to clear arrears with private electricity companies (starting Jan 2006). A loan from the World Bank will be requested, reviewing the amount but, in line with a former loan request for the sector that was not considered viable by the Bank due to the country's failure to meet the IMF agreement of year 2003. Consideration will also be given to the possibility of financing the cost of doing-away with Independent Power Producer's contracts, having them compete in the market.

Private sector participation in Ede-Norte/Sur distribution companies.
Studies will be made, actions will be taken and terms of reference documentation will be made available, in order to be ready to conduct an international bidding process to award a performance based management contract of Ede-Este and Ede-Norte (first quarter 2006).

Reforming the regulatory and legal framework of the sector.
An ongoing review of the proper application of the regulatory framework in place will be done, correctives to be implemented as necessary. The legal framework will be reviewed and if need be, proposals for the amendment of laws will be submitted to congress (latest third quarter 2006).

(4.) (U) This report and others can be read on the SIPERNET at <http://www.state.sgov.gov/p/wha/santodomingo/index.cfm> along with extensive other current material.
HERTELL